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VH/MM/B02

EACB Note on
Draft regulatory technical standards on the content of resolution plans and the assessment of resolvability (EBA/CP/2014/16)
and
draft Guidelines on the Specification of measures to reduce or remove impediments to resolvability and the circumstances in which each measure may be applied under Directive 2014/59/EU
(EBA/CP/2014/15)

The members of the EACB welcome the opportunity to comment on the EBA draft RTS on the content of resolution plans and the assessment of resolvability and on draft Guidelines on the specification of measures to reduce or remove impediments to resolvability.

1. ***Comments on the draft RTS***

Choice of preferred strategy

The draft standard makes numerous reference to "preferred" resolution strategy (Art. 4(1)(b)eventually implying the need to establish "alternative" resolution strategies.

We consider that it is not practical to develop simultaneously several resolution strategies, which should be used in differing circumstances. In our view there is only one plan sufficient which is developed taking into account all foreseeable conditions. And which is assessed on its practical applicability in all relevant circumstances.

We believe that developing and maintaining several plans at the same time is highly impractical, costly, and resource consuming.

The proposal indicates (Art. 4(1)(b) and Art. 6) that a choice for the resolution plan in Single Point of Entry (SPE) versus Multiple Points of Entry (MPE) has to be made. In our view it is not really practical to constrain the choice between two possibilities which are radically opposed, and to fix this choice as the fundamental point of departure to structure the resolution plan.

As also indicated in the section of the consultation paper on "cost benefit analysis and impact assessment" section under paragraph "Assessment of resolvability depending on number of points of entry", the need for a distinction between SPE resolution approach and MPE approach is not explicitly provided in the level 1 legislation.

In fact, the possibility that a combination of both strategies would more appropriately accommodate the structure and specificities of an institution or a business model could make such distinction hard to be effectively implemented.

For instance, a mixed approach for international operating banks could foresee that to group members within the SSM an SPE approach is applied, while to group members outside the EU an MPE approach is applied, for example due to ring-fencing tendencies and/or the lack of burden-sharing agreements.

Moreover, intra-group funding should already be considered at the stage of assessment of the appropriateness of the resolution rather than at the stage of assessment of the feasibility of a resolution strategy (i.e. in Art.6 rather than Art.7) since:

- intragroup funding (i.e. shareholder loans) is considered as junior loan or even as equity substation under many insolvency laws;
- intragroup funding is almost automatically an eligible liability and carries higher risk than similar liabilities from third parties;
- bailing-in intragroup funding at subsidiary level will protect creditors (and ultimately resolution and DGS funds) at subsidiary level at the expense of creditors at the parent level;
- intragroup funding often is cheaper or the only possible access to such funds (due to maturity, currency, etc.) and may have impact on the business model of the subsidiary.

In the light of the resolution objectives it is more a question of appropriateness rather than a question of feasibility when risk is shifted from creditors of one country to creditors of another country by act of a national authority (i.e. by bailing in intra group funding). Even more so if the problems in the subsidiary arise due to a sovereign crisis or legislative action of the sovereign. Art.6 does not give an indication how to proceed when the matters indicated in para. (3),(a) to f) (availability and enforceability of resolution tools, loss absorbing capacity, intra-group loss-transfer agreements, organizational structure, uncooperative third country authorities) give conflicting signals. This is even more so as resolution objectives referred to in Art. 31 BRRD could prove difficult to reconcile (Bailing in bank and unprotected client liabilities to protect public funds contradicts preventing contagion and protecting client funds).

Reference to "loss absorbing capacity"

We note that the draft standard formally introduces a definition for "loss absorbing capacity" (Art. 2(c)). While there are references, the concept is not formally defined in the BRRD and we believe that the introduction of this concept should be carefully fine-tuned with respect to the obligations stemming from the MREL.

Otherwise it could create uncertainty on the scope of the MREL which is not beneficial both for institutions and investors. Instead, the MREL should be explicitly recognised in this context.

1.1 Answers to specific questions on the draft RTS

Q.1 *Do you agree that this step should be distinguished from the assessment of resolution strategies and carried out first?*

We believe that while this distinction is acceptable in principle it should however be kept in mind that for a larger single institution the assessment is likely to depend on the size of the institution and may require the existence of a valuation for the purposes of resolution in accordance with Art. 36 BRRD which is not available in the planning stage.

It should also be noted that groups cannot be subject to liquidation "under normal insolvency proceedings" but this is applicable only to single members of the group. The question whether to liquidate or resolve the parent institution of a group will therefore depend on the magnitude of the damage incurred in the subsidiary, size of own funds and eligible liabilities available in the parent institution as well as in the subsidiary, intra-group exposures and home/host issues, so that the answer to this question will go hand in hand with Art. 4(b) of the draft RTS on the selection of a preferred resolution strategy.

Finally, while the Sequence of the stages is a logical exercise, in many cases it will could be difficult to distinguish the stages of (a) and (b). In fact within a group the sequence between might even be reversed

Q.2 *Do you agree that this initial stage (preliminary identification of resolution strategies) should be separately identified?*

While it would be necessary to ascertain the prevailing circumstances at the point of unviability to determine the best resolution strategy, the best resolution strategy will also depend on the how well institutions are prepared, although knowing when, where and how the crisis will arise is a difficult exercise. This is probably the most critical aspect of the resolution framework.

Moreover, implementing the consequences for a chosen resolution strategy might take years to implement (e.g. reduction of long term intra group financing to implement an MPE approach) while in the meantime the chosen strategy might not be the best any more.

In case of cross border groups the choice of any resolution strategy in the planning phase will thus much more be a consequence of risk appetite (or lack thereof), and an MPE approach is likely to be the preferred approach for each single resolution authority. However, an MPE strategy might not be the most economical way to handle resolution or ongoing business. Own funds available in the group may lay idle in group members in other countries where they are not needed, but cannot be transferred to entities where they are needed.

Q.6 *Do you have comments on the matters identified under each category?*

The requirement under Art. 7(6)(c) on "The capability of the institution or group to provide information to carry out a valuation to determine the amount of write-down or recapitalisation required […]" seems excessive, especially in connection with collateralized (real estate) loans. It is hard to predict results of cashing collateral in the future. Consequently the amount to be written down will always be an estimate as collateral valuation may prove difficult in a crisis. This should not determine the resolution strategy. We believe that this requirement should be deleted.

We believe that Art. 7(7)(b) on the "Existence of adequate processes for coordination and communication and assurances on actions to be taken between home and host authorities, including in third countries, to enable delivery of the resolution strategy." Should be amended to refer only to cooperation with third country States. A cooperation between home and host authorities within the EU is a precondition for a working Banking Union. This comment would also apply to Art.6(f) in connection with EU authorities not refraining from independent resolution actions.

Finally, application of Art. 7(8)(b) may require the change of ISDA documents and similar as the BRRD is only applicable within the EU.

2. ***Comments on the draft GL***

Comments on proportionality

We welcome the introduction of an explicit consideration of the proportionality principle to mitigate the measures mentioned in Art. 17(5) BRRD, which could not only have a disproportionate impact but also conflict with property rights or the four freedoms of the EU. It should be considered that institutions may become not viable not only due to own mistakes, but also due to sovereign failures. Therefore, similar to Recital 13 of the BRRD, a referral to the EU Charter of Fundamental Rights of the European Union should be included in the Guidelines as well. This would imply that also resolution authorities would be bound by the Charter.

Asset divestment

Para. 10 of the draft GL makes reference to the possibility for resolution authorities to require institutions to divest from certain assets already before the resolution case, based on an assessment of their liquidity. We believe that this requirement should be more carefully tuned, in particular due to the multifaceted nature of liquidity.

Q.2 *Do you see further cases for applying this measure? How can the asset structure of institutions be improved?*

With regard to the application of the measures under Art. 10, we would like to highlight that often for groups some of the most valuable assets are participations in subsidiaries. Such participations, however, are in many cases assets "the sale of which in the timeframe provided for under the resolution strategy is likely to result in pressure on prices for assets, destruction of value and additional uncertainty and vulnerability of financial markets and other institutions […]". In this context, the requirement to sell a (foreign) subsidiary in the planning phase because the sale of such subsidiary could pose a problem during resolution is a far reaching decision. The draft Guidelines should provide more and clearer details than those given. The legal determination for such passage seems insufficient.

Moreover, the requirement to divest specific assets will most likely destroy value for these assets as the market will be aware of the pressure to sell. Consequently, such action should comply with EU Charter of Fundamental Rights of the European Union as it may be regarded – at least in the amount of such devaluation – as an expropriation.

Q.4 *Do you agree with the description of the potential advantages of a financial holding company structure? Do you see any disadvantages of this structure as regards financial stability?*

We believe that the requirement under para. 14(b) is extremely intrusive as it touches upon the very process of governance of institutions. In particular, it does not take into account, the specificities of the cooperative groups and networks, and the existence of cooperative solidarity mechanisms, which leaves some doubt on the applicability of such guidelines to cooperative banks.

These are characterised by an inverse pyramid structure where the local banks are the shareholders of central institutions that perform a number of activities in account of the whole group (e.g. capital market access and central bank operations, liquidity management, payment services etc). In this context the creation of a financial holding structure would be extremely complex and prove hardly beneficial.

We believe that such structural issues should be discussed in connection with the proposal for a regulation on structural measures improving resilience of EU credit institutions. In this respect, any pre-emptive rule should be avoided.

It should also be reminded that in many jurisdictions shareholder loans are treated akin to equity or with similar ranking. Consequently any senior, but bail-inable loan from an intermediate financial holding company channelled to the operative company will turn subordinate or *pari-passu* with AT1 or T2 at the level of the operative company. This will have to be considered in light of the no creditor worse off principle (i.e. it cannot be ignored in the case of insolvency of the operative company) and thus make any bonds issued by the interim financial holding much more expensive than a bond issued by the operative company as they carry more risk.

Any requirement to set up an interim holding within EU could be considered as measure to protect EU banks from foreign competition and may only be appropriate as a retaliatory action for jurisdictions requiring the same.

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